



Investment Office
P.O. Box 2749
Sacramento, CA 95812-2749
Telecommunications Device for the Deaf - (916) 795-3240
(916) 795-3400

May 12, 2008

AGENDA ITEM 8a

TO: MEMBERS OF THE INVESTMENT COMMITTEE

- I. SUBJECT:** Emerging Markets Program Manager Reports
- II. PROGRAM:** Global Equity
- III. RECOMMENDATION:** Information only

Current Emerging Markets Managers

AllianceBernstein	Genesis Asset Managers
Batterymarch Asset Managers	Lazard Asset Managers
Dimensional Fund Advisors (DFA)	Pictet Asset Managers

IV. ANALYSIS:

Executive Summary

This is the annual presentation of the emerging markets manager reports. This is the first update since the prior nineteen factors used for implementing CalPERS emerging markets equity program were organized into eight Emerging Equity Markets Principles and quantified into a formal policy adopted November 13, 2007 effectively repealing the prior policy, Permissible Equity for Emerging Equity Markets. The policy is Attachment 1.

The performance of the external emerging markets equity managers has been positive, outperforming the custom benchmark on an annualized basis by 1.81% from inception on August 1, 2002 through the period ending March 31, 2008. The custom benchmark has been updated to reflect the broader permissible universe of countries, based on the updated policy.

During the last twelve months, three new managers have been added to the program to provide additional diversification. Accordingly, allocations to each of CalPERS' three existing external emerging markets managers were reduced, at least in part, to fund the three new emerging markets managers: Batterymarch Financial Management, Lazard Asset Management, and Pictet Asset Management. Batterymarch and Pictet were funded on June 1, 2007 and Lazard was funded on August 1, 2007. Batterymarch, Lazard, and Pictet were part of a pool of emerging markets managers approved by the Investment Committee at its May 15, 2006 meeting.

Several documents are included in this item. Attachment 2 contains the presentation slides from each of the seven firms that will be discussed with the Investment Committee. Attachment 3 contains an overview of KLD Consulting's Emerging Markets Research Methodology. Attachment 4 contains the external manager reports that detail their investment process and consideration of the CalPERS Emerging Equity Market Principles, a fundamental component of these investment mandates. Staff will also make available upon request the full list of holdings, and information on how the Principles are applied to the holdings, for each of the managers. Due to the large amount of paper, staff did not include this information with the item.

Staff looks forward to receiving the Investment Committee's feedback and insights on these reports and presentations, so staff can continue to work with the managers to improve this process.

Background

At its November 13, 2000 meeting, the Investment Committee approved a recommendation to: (1) hire active emerging market equity managers who can demonstrate a transparent and well documented process for incorporating strategic factors to support CalPERS' emerging equity program; and (2) require annual reporting to the Investment Committee on the application of the required strategic factors considered for investing CalPERS' portfolios.

After a workshop at the May 14, 2007 Investment Committee meeting and discussion of additional information presented at the June 18, 2007 Investment Committee meeting, refinements were made by the Investment Committee at the August 13, 2007 meeting. The Investment Committee decided to continue the principles based emerging markets investing approach without separately approving individual countries. Previously, Wilshire Associates, with comprehensive detailed data from several providers, compiled a complicated decision matrix scoring and ranking each emerging market country.

CalPERS' external emerging markets program consists of six managers. Alliance Bernstein, DFA, and Genesis were funded August 1, 2002. Batterymarch Financial Management and Pictet Asset Management were funded on June 1, 2007. Lastly, Lazard, was funded on August 1, 2007. As required in CalPERS Emerging Equity Markets Principles policy, the emerging markets managers' annual report includes the incorporation of CalPERS' Principles in the management of their CalPERS portfolio: a list of the data sources used in evaluation of these principles, a description of how these principles are incorporated in the manager's investment process, a report of any countries that are cause for concern due to one or more of CalPERS' Principles, and a rationale for any investments made or held in those countries if securities in those countries are not completely excluded.

Two managers, Alliance Bernstein and DFA have engaged the services of KLD Consulting, which offers specialized research solutions and support services, particularly customized offerings, to enhance their own efforts in applying CalPERS' Emerging Equity Market Principles. Presently KLD is providing data and custom screening input tailored specifically to these principles and the managers' unique investment processes.

Recently, CalPERS has extended this relationship with KLD to provide a completely screened investable universe to support CalPERS' internal emerging markets public equity investing program, approved by the Investment Committee at its March 2008 meeting. KLD offers in-depth data and comprehensive screening capabilities with the scope and flexibility to meet CalPERS needs. More detailed information can be found in Attachment 3.

Assets under Management

As of March 31, 2008, approximately \$5.8 billion is being managed by the external emerging markets managers reviewed in this agenda item. Table 1 shows the assets managed by each manager as of this date.

Table 1

Manager	Portfolio Value (in \$ millions)
AllianceBernstein Institutional	1,332.0
Batterymarch Financial Mgmt.	572.0
Dimensional Fund Advisors	1,340.8
Genesis Asset Managers	1,372.0
Lazard Asset Management	590.0
Pictet Asset Management	566.8
Total Active Emerging Mkts Equity	5,773.6

Source: State Street Bank

Performance

The actively managed portfolios' performance objective is to exceed the benchmark returns, net of management fees, over a full market cycle that is considered to be three to five years. Table 2 displays the total emerging markets external managers' active composite returns over three- and five-year annualized periods relative to the custom benchmark. Staff did not show the individual performance of the managers since it will be presented during the annual international program review in the fall. Staff will be prepared to discuss individual manager performance at the meeting.

Table 2

Emerging Markets Performance	3-Year Annualized	5-Year Annualized	Since Inception
Active Emerging Markets Portfolio	26.96%	36.45%	29.67%
Benchmark	28.28%	34.90%	27.86%
Active Return	(1.32%)	1.55%	1.81%

Source: State Street Bank. Returns are net of fees and CFA compliant. Returns are as of 3/31/08.

The last twelve months have been characterized by market uncertainty and the CalPERS Emerging Markets Equity Active portfolio returned 18.63% underperforming the custom benchmark of 20.35% by 1.72%. However, since inception of August 2002 through March 2008, the total active portfolio outperformed its benchmark by 1.81% on an annualized basis. Note all returns in this report are net of management fees and are CFA Institute compliant.

Attached Documents

Attachments are as follows: Attachment 1, presentation materials of involved external parties; Attachment 2, details of KLD screening process in preparing an investable universe for CalPERS' Internal Emerging Markets Program; and Attachment 3, external manager reports.

V. STRATEGIC PLANS:

External investment manager performance is monitored by staff and reported to the Investment Committee per CalPERS Strategic Plan, Goal VIII to manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits and second, to minimize and stabilize contributions.

VI. RESULTS/COSTS:

No additional costs have been incurred by CalPERS as a result of this program in the last twelve months.

Sheila Halousek
Investment Officer

Kurt Silberstein
Senior Portfolio Manager

Eric Baggesen
Interim Senior Investment Officer

Anne Stausboll
Interim Chief Investment Officer